To Mr Alan Worsley
Senior Specialist, Strategic Policy
Australian Securities and Investments Commission
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07 August 2019

Dear Mr Worsley,

RESPONSE TO ASIC CONSULTATION PAPER 315: FOREIGN FINANCIAL SERVICES PROVIDERS (FFSP): FURTHER CONSULTATION

1 Introduction

The Association of the Luxembourg Fund Industry (**ALFI**) appreciates the opportunity to comment on the proposed changes regarding the regulation of foreign financial services providers in ASIC Consultation Paper 315: *Foreign financial services provider: further consultation* (**CP 315**).

ALFI is the representative body of the Luxembourg investment fund community. Created in 1988, ALFI today represents over 1,400 Luxembourg domiciled investment funds, asset management companies and a wide range of service providers such as depositary banks, fund administrators, transfer agents, distributors, legal firms, consultants, tax experts, auditors and accountants, specialist IT providers and communication companies. Luxembourg is the largest fund domicile in Europe and the Luxembourg funds industry is a worldwide leader in cross-border fund distribution. Luxembourg domiciled investment structures are distributed in more than 70 countries around the world.

In 2013, ALFI applied for class order relief from the requirement for CSSF-regulated financial services providers[1] to hold an AFS licence in respect of financial services provided to wholesale clients only in Australia. AFS licensing relief was granted by ASIC on 8 November 2016 under *ASIC Corporations (CSSF-Regulated Financial Services Providers) Instrument 2016/1109* (**Instrument 2016/1109**).

We believe that this licensing relief regime provided an appropriate way to facilitate cross-border investment while ensuring investor protection, as it offers Australian wholesale clients efficient access to financial products from jurisdictions that have been assessed as having regulatory frameworks that are sufficiently equivalent to the framework in Australia. Instrument 2016/1109 has enabled significantly easier access to UCITS[2] initiated by fund managers regulated by the CSSF in Luxembourg.

[1] As defined in *ASIC Corporations (CSSF-Regulated Financial Services Providers) Instrument 2016/1109*.

[2] "UCITS" means Undertakings for Collective Investment in Transferable Securities.

The UCITS concept is originally derived from the European Directive 85/611/EC, replaced by European Directive 2009/65/EC (the **Directive**), which provides a single regulatory regime across the European Union for open-ended funds investing in transferable securities such as shares and bonds.

One of the primary objectives of the UCITS regime is to harmonise collective investment schemes in the EU through the introduction of a common investment vehicle which can be established and regulated in one EU Member State and marketed across the EU without the need for further authorisation (i.e. the so-called "passport"). With a view to defining the highest levels of investor protection and in recognition of the UCITS' retail nature, the Directive regulates the organisation, management and oversight (including conduct of business rules) of such funds, while imposing rules concerning diversification, liquidity and use of leverage, among other items. More recently, as from March 2016, the Directive also sought to harmonise further the provisions in respect of UCITS fund depositaries, specifying safe-keeping duties, asset protection standards via appropriate segregation requirements, as well as a strong liability regime in the event such rules were to be breached.

The UCITS brand is recognized as a true globally distributed investment fund product, and a growing number of countries in Asia and Latin America have accepted UCITS as providing a stable, high quality, well-regulated investment product with significant levels of investor protection. Given such guarantees, local authorities have been traditionally comfortable in permitting the sale of UCITS to retail investors in their respective jurisdictions outside the EU. Today, UCITS are marketed on a global basis in more than 70 countries with a particular focus on Europe, Asia, Latin America and the Middle East. As a result, many asset managers are establishing UCITS funds with a clearly defined global distribution strategy.

We are pleased to provide you with comments on the following questions:

B1Q1 Overall comment

We welcome ASIC's proposal to provide relief to permit FFSPs to provide funds management financial services to professional investors. Indeed, we believe it is important for Australian professional investors, including superannuation funds, to have access to a broad range of funds management expertise to deliver diversified returns for their investors and shareholders.

As ASIC notes in the Key Points in Section B of CP 315, many FFSPs that provide funds management services are not able to rely on other kinds of relief or exemptions. For this reason, narrowing the existing relief too far could result in a reduction in the investment management options available to Australian professional investors. We therefore agree with ASIC that it is very important to develop rules which strike the appropriate balance between cross-border facilitation, investor protection and market integrity.

B1Q2 Custodial and depositary services

We do not agree with ASIC's proposal not to provide relief in relation to the provision of a custodial or depositary service on the basis that it is covered by reg 7.6.01(1)(k).

Reg 7.6.01(1)(k) only applies in the specific circumstance where the FFSP is acting as a sub-custodian. This is unreasonably limiting on smaller FFSPs (who may not be able to engage an AFS licensee as custodian) and limits the ability of Australian investors to choose the most appropriate custodian.

Due to the definition of custodial or depository services under section 766E(3)(b) (which excludes holding the assets of a registered scheme), this relief may also not apply where the Responsible Entity of a registered scheme invests in an offshore fund. We therefore think that the relief should cover custodial or depositary services expressly in order to achieve the policy objective.

B2Q2 Definition of "portfolio management services"

We recommend not to limit the scope of "portfolio management services" to "assets located outside Australia". We submit that the definition of "portfolio management services" should be broadened to include the management of any assets by a foreign manager.

CP 315 (para 42) refers to the relief being intended to cover the situation "*where funds management services are primarily concerned with financial service in relation to offshore interests and securities*". However, the current drafting could be interpreted to mean that a global equities portfolio would not be within the scope of the relief because it included one or more Australian equities. Global equities mandates often have a component of Australian equities. We submit that the relief should allow for portfolio management services or investments in Australian securities as this may be an incidental part of the overall portfolio (for example, in a global mandate).

We also submit that the definition should be expanded to cover "management of assets (including related dealing services and financial product advice)" as portfolio managers generally also provide reporting and commentary, which may be financial product advice, and dealing services which relate to portfolio management.

B2Q3 Eligible Australian Users

We propose that portfolio management services should be able to be provided to existing categories of "wholesale investors" or "professional investors" rather than creating a new category of "eligible Australian users".

We think that this better meets Recommendation 7.3 of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services (**Royal Commission**) that laws and regulation should be kept as simple as possible and exceptions and carve-outs to otherwise generally acceptable norms of conduct reduced.

Creating a new legal category of investors increases the complexity and compliance burden on ASIC to monitor the use of this relief as well as users of the relief and the eligible Australian users themselves. We do not consider that there is a different consumer protection risk for portfolio

management services when compared to dealing in the interests of a managed investment scheme or securities of a body that carries on a business of investment. Portfolio management services may be engaged by a professional investor such as a family office (a private wealth management advisory firm that serves ultra-high net worth investors) or a listed investment company that is excluded from the benefit of the proposed relief.

In the alternative, if a newly created sub-set of professional investors like the "eligible Australian user" is created, it is submitted that its definition should be widened: other types of professional investors should be included, such as family offices and listed investment companies who would need the benefit of access to a diverse range of investment managers for the same reasons as the identified "eligible Australian users".

Secondly, it is also not clear whether the relief covers the scenario where an offshore manager offers its portfolio management services through an Australian managed investment scheme:for example, the offshore manager provides services to a responsible entity as a professional investor). We would request that ASIC please clarifies whether the relief is intended to cover this scenario.

B3Q1 Aggregated revenue cap

We think that it is important that any cap applied must be practical and give certainty to Australian professional investors engaging an FFSP as well as the FFSP itself. Australian professional investors typically engage a portfolio management service or invest in a vehicle for a long period of time (i.e. exceeding one year and often for several years) and need certainty of the licensing or relief/exemption status of the provider.

Likewise, for a FFSP to enter into such an agreement with an Australian professional investor, they need certainty of their compliance arrangements. The proposal in draft RG176.122 means that there is a degree of uncertainty for both parties when they enter into such an arrangement based on this relief, as on an annual basis the compliance arrangements may need to change. It may result in losses to Australian clients if an FFSP relying on the relief was forced to suddenly terminate their arrangements due to the relief ceasing to apply due to circumstances outside of their control.

By way of example:

- the proposed cap could be exceeded as a result of market movements or by a reduction in the FFSP's business outside Australia. If there was a large redemption from a fund or the termination of a significant mandate outside Australia, it could cause the proportion of revenue from Australian investors to increase as a proportion of total revenue.
- a foreign financial services provider may be part of a corporate group that has operations in Australia that may trigger the cap. It could also be triggered by a performance fee in a particular year.
- the proposesd cap would also seem to benefit larger global managers rather than smaller managers. A large manager would have more aggregate group revenue, and therefore a larger 10% cap. This affects the ability for smaller FFSPs to compete, and undul restricts competition for offshore managers in the Australian market.

For these reasons, we propose that compliance with the 10% revenue cap be assessed at the time that an offer is first made to a particular professional investor for a portfolio management service and at the time of the first offer to a new professional investor in an investment vehicle.

We also submit that the cap should be assessed on the revenue of the corporate group, excluding any services provided under an AFSL by a related party entity. This assessment should be made for the first investment.

Where an investment vehicle is a separate legal etity, the aggregated cap should not be applied to that particular investment vehicle and its group, but to the revenue attributable to the services provided by the manager or sponsor of the vehicle (and its corporate group as a whole).

The cap as currently drafted restricts the ability of Australian professional investors to invest in a diverse range of smaller investment vehicles. If the revenue cap was to be applied in this way, it would significantly undermine the effectiveness of the relief.

B3Q2 Systems and processes to monitor compliance

As outlined above, it is not practical for compliance to change from year to year based on a revenue test as businesses need certainty to promote and engage investment management services for the long term. We think that the process of constant reassessment, as outlined in CP 315, does not meet recommendation 7.3 of the Royal Commission report, as it creates unnecessary complexity.

We would recommend the implementation of an appropriate mechanism by which affected FFSPs can address any potential excess of the revenue cap without damage to their business and/or their clients. As noted above, a reasonable adjustment period might be helpful or the ability of the business to discuss their case with an ASIC officer who is authorised to agree temporary exemptions from the strict limits of the cap on a case by case basis (conditionally or unconditionally).

B3Q3 Costs to implement

The major cost of the proposal in RG176.122 is that it puts current and future business at risk. We think that a professional investor should be able to engage a FFSP for a long term contact on the basis of this relief, regardless of changes to the FFSP's business in any given year.

B4Q1 Conditions

First, we submit that a FFSP should not be prevented from relying on the relief as a result of itcarrying on business in Australia. In our experience, whether a person is carrying on business in Australia is a complex question of fact, not easily answered through legislation or case law. The purpose of the FMFS relief is to permit certain activities. This provides the unsatisfactory result that an entity, in undertaking these **permitted** activities, could be be taken to be carrying on business in Australia, and therefore be precluded from relying on the relief. This potentially negates the usefulness of the relief.

We think that there are already sufficient conditions on the relief to ensure it is targeted at offshore FFSPs. At present, an entity relying on sufficient equivalence relief, that is taken to be carrying on

business in Australia, must also register as a foreign company. We submit that there are no reasons why the same approach cannot apply to the FMFS relief.

Secondly, as noted above, we submit that the relief should allow for portfolio management services or investments in Australian securities as this may be an incidental part of the overall portfolio (for example, in a global mandate).

C1Q1 Reverse solicitation

We submit that ASIC should provide an exemption based on reverse solicitation as the current exemption in reg 7.6.02AG is restricted to certain products and services.We submit that a reverse solicitation exemption should apply broadly for services provided only to professional investors so Australian professional investors can have confidence that approaching a FFSP for its services (in the context of reverse solicitation) will pose no regulatory problems in itself.

Grandfathering

We submit that there should be grandfathering for entities relying on existing limited connection relief to avoid the situation where the FFSP that does not apply for a licence and does not otherwise qualify for relief is forced to terminate existing Australian clients through a compulsory redemption of interest, which could be to the detriment of those Australian clients or their underlying investors. Examples of such FFSPs include businesses that continue to provide a custodial or depositary service or a dealing service to Australian wholesale clients as the operator of a foreign fund.

We propose therefore that services provided to existing Australian clients under existing arrangements where the FFSP was relying on the limited connection relief should be grandfathered by way of a continuing exemption.

We trust this submission is useful for ASIC's policy formulation. Please do not hesitate to contact Mr. Pierre Oberlé, Senior Business Development Manager at ALFI ([redacted]) should you wish to discuss it further.

Yours sincerely

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